

STATE OF ILLINOIS

ILLINOIS COMMERCE COMMISSION

Utility Services of Illinois, Inc.	:	
	:	
Proposed Rate Increases for Water	:	14-0741
and Sewer Service.	:	

PROPOSED ORDER

August 7, 2015

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PROPOSED ORDER

By the Commission:

I. INTRODUCTION

A. Procedural History

On November 10, 2014, Utility Services of Illinois, Inc. (“USI” or the “Company”) filed tariff sheets with the Illinois Commerce Commission (“Commission”), pursuant to Section 9-201 of the Public Utilities Act (“Act”). In these tariff sheets – ILL.C.C. No. 3 First Revised Title Sheet, First Revised Sheet Nos. 1 through 4 and ILL.C.C. No. 4 First Revised Title Sheet, First Revised Sheet Nos. 1 and 2 – USI proposed a general increase in rates for water and sewer service as well as other proposed changes.

Notice of the proposed changes reflected in the tariff sheets was sent to customers, posted in USI’s business offices, and published in a newspaper of general circulation in its service areas, in accordance with the requirements of Section 9-201(a) of the Act and the provisions of 83 Ill. Adm. Code Part 255. The Commission issued an Order on December 17, 2014 suspending the tariffs up to and including April 10, 2015 and initiating this proceeding. Subsequently, the Commission re-suspended the tariffs on March 25, 2015 up to and including October 10, 2015.

On December 19, 2014, the Attorney General of the State of Illinois (the “AG”) filed an appearance. On January 16, 2015, the Company filed a Motion for Entry of a Protective Order in this proceeding, which was granted on February 18, 2015. On January 6, 2015, the Galena Territory Association (“GTA”) filed a verified petition to intervene. On April 23, 2015, Westlake Village Master Homeowners Association, Inc. (“WVMHA”) filed a verified petition to intervene. On April 30, 2015, Westlake Village Limited Partnership (“WVLP”) filed a verified petition to intervene. On July 6, 2015, Lake Holiday Property Owners Association, Inc. (“LHPOA”) filed a verified petition to intervene. All of the petitions were granted.

Pursuant to notice as required by the law and rules and regulations of the Commission, an evidentiary hearing was held before a duly authorized Administrative Law Judge (“ALJ”) of the Commission at its offices in Chicago, Illinois on May 20, 2015. At the evidentiary hearing, the Company, the AG, Staff of the Commission (“Staff”), GTA, WVMHA, and WVLP (collectively, GTA, WVMHA, and WVLP are the “Intervenors”), appeared and presented testimony.

The Company presented the following witnesses: Steven Lubertozzi, President of USI; Dimitry I. Neyzelman, a Financial Planning and Analysis Manager at Utilities, Inc. ("UI"); Justin Kersey, the Financial Planning and Analysis Manager of USI; Bruce T. Haas, Vice President of Operations for the Midwest Region of UI; John F. Guastella, President of Guastella Associates, LLC; and Dylan W. D'Ascendis, a Managing Consultant at Sussex Economic Advisors, LLC.

The following witnesses testified on behalf of Staff: Richard W. Bridal II, Mary H. Everson, and Theresa Ebrey, Accountants in the Accounting Department of the Financial Analysis Division; Christopher Boggs, a Rate Analyst in the Rates Department of the Financial Analysis Division; Janis Freetly, a Senior Financial Analyst in the Finance Department of the Financial Analysis Division, Jonathan M. Sperry, a Water Engineer in the Water Engineering Program of the Safety and Reliability Division; and Michael McNally, a Senior Financial Analyst in the Finance Department of the Financial Analysis Division.

The Intervenor presented the following witnesses: Joe Mattingley, the Chief Executive Officer of GTA on behalf of GTA; Steven Korn, a member of the board of directors of WVMHA on behalf of WVMHA; and Timothy H. Jagielski, the Assistant Counsel at Williams Charles, Ltd. on behalf of WVLP. The AG presented the testimony of Frank W. Radigan, a Consultant at Hudson River Energy Group.

Initial Briefs and Reply Briefs were filed by all of the parties, except LHPOA, on June 16, 2015 and July 7, 2015, respectively. On July 17, 2015, Staff filed a Motion to Deny Requests for Public Forum, which was granted on August 3, 2015. The record was subsequently marked "Heard and Taken."

B. Nature of Operations

USI is a wholly owned subsidiary of UI. UI owns approximately 63 water and sewer utilities operating in 15 states, including USI. Water Service Corporation ("WSC") manages the operation for all of UI's water and wastewater systems, including USI. WSC provides management, administration, engineering, accounting, billing, data processing, and regulatory services for the utility systems. WSC's expenses are assigned directly to a utility or distributed to the various companies pursuant to a formula that has been approved by the Commission.

USI was incorporated in 2013 solely for implementation of the merger into a single entity of the 23 separate wholly owned subsidiaries of UI that provided water and sewer services in Illinois (the "Illinois Utilities"). The merger was approved by the Commission on October 7, 2014 in Docket No.13-0618. Under the approved merger, the existing rates of each of the Illinois Utilities remained in effect for the customers located in divisions of USI corresponding to the service areas that were served by the former UI operating subsidiaries. More than half of those utilities had not filed for a general rate increase since 2010, and the rates for six of those companies were established during the period from 1987 through 2004. For most of the predecessors that filed for rate increases after 2010, the current rates were designed to recover expense levels based on test years that included costs incurred in 2010.

USI provides water service to approximately 12,000 customers and almost 3,000 availability customers via almost 50 wells and more than 1.39 million (“mm”) linear feet of water distribution mains. USI also provides wastewater service to approximately 4,000 customers via more than .240 mm linear feet of wastewater collection mains and seven wastewater treatment facilities. USI serves customers in twelve different counties throughout Illinois, including Jo Daviess, Kane, Lake, LaSalle, Marshall, McHenry, Peoria, Stephenson, Vermilion, Will, and Winnebago.

C. Test Year

USI's filing is based on a future test year ending December 31, 2015, with pro forma adjustments for known and measurable changes. No party challenged the reasonableness of using the year 2015 as a future test year.

The Commission concludes that the test year ending December 31, 2015, with adjustments for known and measurable changes, is appropriate for the purposes of this proceeding.

D. Requested Increase

USI originally proposed to increase annual revenues by \$2,326,239 for water service and \$576,917 for sewer service. In surrebuttal testimony, USI proposed a \$2,061,306 revenue increase for water and \$533,552 increase for sewer which reflects that USI agreed with or accepted, in whole or in part, numerous Staff and AG proposed adjustments and updated certain items.

II. RATE BASE

A. Uncontested Issues

1. Working Capital

Staff witness Ebrey proposed an adjustment to the Company's proposed calculation of cash working capital to remove the impact of real estate taxes where payment is deferred for more than one year because the deferral results in an extended payment lag from which the Company has the use of the funds. Staff Ex. 1.0 at 7-8. The Company accepted Staff's adjustment. USI Ex. 7.0 at 1-2.

The Commission finds that this adjustment is appropriate.

2. Plant Disallowances from Prior Proceedings (Including Derivative Impacts)

Staff proposed an adjustment to remove certain plant that had previously been disallowed in prior rate cases of Del-Mar Water Company and the derivative adjustments for that plant. Staff Ex 3.0 at 2. The Company accepted Staff's adjustment. USI Ex. 7.0 at 2 and Scheds. 7.02 W and 7.04 W.

The Commission finds that adjustment to be appropriate.

3. Capitalized Time in Plant Accounts with No Assets

Staff witness Ebrey proposed an adjustment to remove capitalized labor associated with plant accounts 307 and 335 because there were no assets in those

accounts. Staff Ex. 3.0 at 3-4. The Company accepted Staff's adjustment. USI Ex. 7.0 at 2 and Scheds 7.02 W and 7.04 W.

The Commission finds that Ms. Ebrey has correctly analyzed this issue and her position is adopted.

4. Derivative Impact of Illinois State Income Tax Rate Change

Staff proposed an adjustment to reflect the impact on accumulated deferred income taxes ("ADIT") for the decrease in the Illinois state income tax ("SIT") rate from 9.5% to 7.75% effective January 1, 2015, in accordance with Public Act 98-496. Staff Ex. 1.0 at 9-10. The Company accepted Staff's adjustment. USI Ex. 7.0 at 8. No other party addressed this issue in testimony.

The Commission finds that adjustment to be appropriate.

5. Derivative Impact of 2014 Bonus Depreciation

Staff proposed an adjustment to reflect the impact on ADIT of the 50% bonus depreciation that the Company elected in 2014. Staff Ex. 1.0 at 12-13. The Company agreed with Staff's adjustment and updated the adjustment to include the impact of changes in 2014 utility plant in service (as set forth in USI Exhibit 7.0, Schedule 7.11 W) and to use the correct SIT rate of 7.75% as opposed to the 9.5% that was used in the calculation of Staff's adjustment. USI Ex. 7.0 at 3; USI Ex. 8.0 at 1-2. Staff concurs with the updated adjustment proposed by USI. Staff Ex. 7.0 at 6. No other party addressed this issue in testimony.

The Commission finds that adjustment to be appropriate.

6. Oakwood Main Project

USI proposed adjustments in its rebuttal testimony to include a major water main project for the Oakwood service area. USI Ex. 7.0 at 2; USI Ex. 9.0 at 1-3. USI first discussed this plant addition in its December 22, 2014 supplemental direct testimony, USI Exhibit 5.01, wherein USI stated that the project was expected to be completed by the end of 2014 and was unintentionally left out of USI's direct testimony exhibits. USI Ex. 5.01 at 1-3. Staff reviewed supporting documentation for the main project and did not object to the inclusion of the project in rate base. Staff Ex. 7.0 at 7. No other party addressed this issue in testimony.

The Commission finds that adjustment to be appropriate.

7. Capitalization of Costs Associated with 83 Ill. Adm. Code 280

In its original response to a Staff data request, Staff DR RWB 3.02, the Company indicated that it intended to include costs associated with the implementation of 83 Ill. Adm. Code 280, Procedures for Gas, Electric, Water and Sanitary Sewer Utilities Governing Eligibility for Service, Deposits, Billing, Payments, Refunds and Disconnection of Service, in its test year forecast. In the Company's supplemental response to Staff DR RWB 3.02, the Company stated that in order to ensure compliance with the rule changes to 83 Ill. Adm. Code 280 it will spend \$643,140 which will be capitalized to computers and depreciation over eight years, resulting in an increase to the Company's depreciation expense of \$80,393. Staff Ex. 1.0 at 21-22. Staff's direct testimony required that if USI

intended to request recovery of these costs, the Company should in its rebuttal testimony clearly set forth the necessary changes to its proposed revenue requirement and provide a detailed explanation of these additional costs. USI provided the required explanation in its rebuttal testimony and referenced its responses to Staff DRs RWB 7.01-7.03 which were outstanding at the time Staff's direct testimony was prepared. USI Ex. 7.0 at 2-3; USI Ex. 6.0 at 5-6. Staff has no objection to including the proposed costs required to implement and comply with changes to 83 Ill. Adm. Code 280. Staff Ex. 7.0 at 8. No other party addressed this issue in testimony.

The Commission finds these adjustments to be appropriate.

8. Original Cost Determination

Based on the adjustments to plant in service recommended by Staff and as calculated on Schedule 1.15, Staff recommended that the Commission Order include the following language:

IT IS FURTHER ORDERED that the \$37,241,560 original cost of water plant in service for Utility Services of Illinois, Inc. at December 31, 2013, as reflected on Staff Schedule 1.15, is unconditionally approved as the water original costs of plant.

IT IS FURTHER ORDERED that the \$11,760,334 original cost of sewer plant in service for Utility Services of Illinois, Inc. at December 31, 2013, as reflected on Staff Schedule 1.15, is unconditionally approved as the sewer original costs of plant.

Staff used December 31, 2013 for the original cost determination because the twelve months ending December 31, 2013 represents the most recent calendar year for which final historical data is available. Because USI maintains its books on a calendar year basis, using the most recent calendar year for which final historical data is available would set a more reasonable starting point for updating the original cost determination in future rate cases. Due to its acquisition during 2014, the Galena Territories–Oakwood service area was not included in Staff's original cost recommendation. Staff Ex. 1.0 at 21-22. The Company agreed with Staff's recommendation. USI Ex. 7.0 at 3. No other party addressed this issue in testimony.

The Commission finds Staff's recommended language is appropriate and should be included in the Ordering paragraphs.

B. Contested Issues

1. Deferred Charges

The impact on rate base of the contested operating expense issue concerning deferred maintenance expense is discussed in Section III.B.1 of this Order.

C. Commission Analysis and Conclusion

The development of the approved water rate base adopted for USI for purposes of this proceeding is shown in Appendix A to this Order, while the approved sewer rate base adopted for the Company is shown in Appendix B to this Order.

The Commission finds that the adjustments to the rate base reflected in the appendices are supported by the evidence, are reasonable, and should be adopted.

III. OPERATING EXPENSES

A. Uncontested Issues

1. Add-On Taxes / Public Utility Tax

Staff proposed an adjustment to remove add-on taxes from operating revenues and expenses. Additional amounts of add-on tax included in the Company's proposed increases were removed through the gross revenue conversion factor on column (f) of Schedules 1.01 W and 1.01 S. The taxes are an add-on charge to customers' bills and are not an actual operating expense of the utility. Staff Ex. 1.0 at 8. The Company agreed with Staff's adjustment. USI Ex. 7.0 at 1-2. No other party addressed this issue in testimony.

The Commission finds Staff's adjustment to be reasonable.

2. Illinois State Income Tax Rate Change

Staff proposed an adjustment to reflect the impact on the test year expenses at present rates for the decrease in the Illinois SIT rate from 9.5% to 7.75% effective January 1, 2015, in accordance with Public Act 98-496, Income Tax Rate – Section 201. Staff Ex. 1.0 at 9. USI agreed with Staff's adjustment. USI Ex. 7.0 at 8. No other party addressed this issue in testimony.

The Commission finds this adjustment is proper.

3. Lake Marian Loss of Prudent Abandonment Amortization

Staff proposed an adjustment to extend the length of the amortization period for the Lake Marian Water Production Plant Loss of Prudent Abandonment. Staff's adjustment results in a reduction to the annual amortization expense. Staff Ex. 1.0 at 10-11. The Company does not agree with Staff's adjustment; however, for purposes of reducing the number of issues in this proceeding the Company accepted Staff's adjustment. USI Ex. 7.0 at 9. No other party addressed this issue in testimony.

The Commission finds Staff's adjustment to be reasonable.

4. 2014 Bonus Depreciation

Staff proposed an adjustment to include the impact of the calendar year 2014 50% bonus depreciation in the revenue requirement. Staff Ex. 7.0 at 12-13. The Company agreed with Staff's adjustment and updated the adjustment to include the impact of changes in 2014 utility plant in service (as set forth in USI Exhibit 7.0, Schedule 7.11 W) and to use the correct SIT rate of 7.75% as opposed to the 9.5% that was used in the calculation of Staff's adjustment. USI Ex. 7.0 at 3; USI Ex. 8.0 at 1-2. Staff concurs with the updated adjustment proposed by USI. Staff Ex. 7.0 at 6. No other party addressed this issue in testimony.

The Commission finds Staff's proposed adjustment, as updated by the Company, to be reasonable.

5. Holiday Parties, Events & Picnics Expense

Staff proposed in direct testimony the removal of USI's holiday parties, events, and picnics expense because these costs are not necessary for the provision of utility service and should not be recovered from ratepayers. Staff Ex. 2.0 at 10. USI did not oppose this adjustment in its rebuttal testimony. USI Ex. 7.0 at 8.

The Commission finds Staff's adjustment to be reasonable.

6. Customer Service Expense

Staff proposed a reduction to USI's forecasted billing and customer services expense to a more reasonable level as determined by the Company in its response to Staff DR MHE 7.05. Staff Ex. 2.0 at 11-12. USI agreed with the adjustment in its rebuttal testimony. USI Ex. 7.0 at 8.

The Commission finds Staff's adjustment to be reasonable.

7. Unaccounted-For Water Expenses

Staff witness Sperry testified that the amount by which the unaccounted-for water exceeds the maximum as defined by the Company's tariffs is 4.2%. Staff Ex. 11.0 at 3, Sched. 11.03. Given Mr. Sperry's testimony that the Company's unaccounted-for water was in excess of that permitted by the Company's tariff, Staff witness Everson calculated an adjustment to operating expenses of negative \$25,893 to account for excess purchased power and fuel, excess chemicals, and excess purchased water. Staff Ex. 8.0, Sched. 8.03. USI did not oppose Mr. Sperry's testimony nor Ms. Everson's proposed adjustment. USI Ex. 13.0 at 5.

The Commission finds Staff's adjustment to be reasonable.

8. Rent Expense

Staff proposed an adjustment to reduce the level of the rent expense based on a more reasonable rate per square foot for the proposed new lease than the rate per square foot proposed by the Company. Staff Ex. 2.0 at 8-10. The AG's proposed adjustment eliminated the increased rent expense that its witness determined to be unsupported. AG Ex. 1.0 at 6. At the evidentiary hearing, USI accepted the AG's adjustment, eliminating the increase to rent expense in its entirety, thus making Staff's proposed adjustment moot.

The Commission finds the AG's adjustment to be appropriate.

9. Rate Case Expense

a. Legal Fees

Pursuant to Section 9-229 of the Act, the Commission is to "specifically assess the justness and reasonableness of any amount expended by a public utility to compensate attorneys or technical experts to prepare and litigate a general rate case filing. This issue shall be expressly addressed in the Commission's final order." 220 ILCS 5/9-229. No party, including Staff, proposed an adjustment for legal fees in their testimony or Initial Briefs. The Company proposed legal fees of \$200,000, to which Staff agreed. USI Ex. 7.2; USI Ex. 13.2; and Staff Ex. 2.0, Sched. 8.02 at 3. In the present case, the Company

has chosen outside counsel to represent them in litigation. In response to a data request, the Company provided copies not only of the amount budgeted for outside counsel and his hourly rate, but also detailed hourly billing records and invoices for outside counsel outlining the services performed along with the date and time in which he performed them. The responses were admitted into the record as USI Exhibit 13.2. These expenses appear commensurate with the expected cost of a case of this type.

The Commission finds that the expenses incurred for outside counsel to litigate this proceeding are just and reasonable under Section 9-229 of the Act.

b. Depreciation Study Witness

Staff witness Sperry testified that USI incurred \$15,724 in charges for work related to a depreciation study as of the filing of Staff's rebuttal testimony. Staff Ex. 11.0 at 2. USI estimated a total cost of \$32,000 for the depreciation study, but that estimate assumed approximately \$16,000 in costs related to post filing work (e.g., preparation of rebuttal testimony, testimony at hearings and post hearing briefing). USI Ex. 7.2, Part 1. Given that the depreciation rates are uncontested, there should be no further costs incurred related to the issue. Therefore, Mr. Sperry recommended that a negative adjustment of \$16,276 be made to rate case expense to reflect actual charges incurred related to the depreciation study. Staff Ex. 11.0 at 2-3, 6. USI agreed with Staff's recommendation. USI Ex. 13.0 at 3.

The Commission finds this adjustment to be reasonable.

c. Rate of Return Witness

Staff proposed an adjustment to rate case expense for USI's rate of return witness's expenses. Staff witness McNally testified that the \$23,956 actually billed for work related to rebuttal testimony was not just and reasonable. Staff Ex. 12.0 at 2. Staff and the Company reached an agreement on the appropriate level of costs for the Company's expert testimony. They agreed that \$20,000 would be a reasonable amount to recover through rates. *Id.* The adjustment is reflected in Staff witness Everson's rebuttal schedules. Staff Ex. 8.0 at 4. The Company confirmed that agreement in the surrebuttal testimony. USI Ex.13.0 at 3.

The Commission finds that the expenses incurred for the costs of the rate of return witness, as modified by the agreement of Staff and the Company are just and reasonable under Section 9-229 of the Act.

d. Mailing, Travel, and Other Costs

Staff proposed an adjustment to USI's forecasted travel to public forums since the Commission did not hold any public forums and none had been planned. Staff Ex. 2.0 at 91-101. The Company incorporated Staff's adjustment into its surrebuttal testimony schedules; therefore it is no longer contesting this issue. USI Ex. 13.0 at 3.

The Commission finds this adjustment to be reasonable.

10. Fuel Expense

Staff proposed a two-fold adjustment to USI's fuel expense to reflect the decline in fuel prices that occurred after USI prepared its fuel forecast and to remove the inclusion

of the 2% escalation factor USI added to its forecast. Staff calculated its adjustment using the U.S. Energy Information Administration Short Term Energy Outlook, dated February 2015. Staff Ex. 2.0 at 2. Staff proposed a fuel expense forecast of \$2.66 per gallon for the 2015 test year based on its calculation. In its surrebuttal testimony, USI accepted Staff's proposal to use \$2.66 per gallon for the projection of the 2015 fuel expense. USI Ex. 12.0 at 2. In its Reply Brief, the AG changed its recommendation stating that it agreed that Staff's recommendation should be adopted because its analysis shows that the 18-month average of gasoline price forecast is \$2.69 per gallon which is comparable to Staff's recommendation. The Intervenor's do not oppose Staff's approach.

The Commission finds Staff's adjustment to be reasonable.

B. Contested Issues

1. Deferred Maintenance Expense

a. Company's Position

USI witness Haas provided descriptions of, the need for, and cost information regarding major deferred maintenance projects that were included in the Company's revenue request. Among other things, these projects included hydro tank inspections, inspection and cleaning of sewer systems, inflow and infiltration research and repair, and hydro tank painting. USI Ex. 5.2.

The Company notes that it accepted Staff's proposed adjustments to deferred maintenance expense. The resulting annual expense supported by Staff and the Company is \$294,440.

The Company complains that AG witness Radigan focused on the overall level of spending rather than specific projects and proposed a blanket adjustment to reduce total deferred maintenance expense to \$300,000. The Company states that it specifically identified the projects that would be performed and the costs (USI Exhibits 5.2 and 5.3), contrary to the AG's incorrect assertion that USI "did not show any reason for such a dramatic increase" in the level of deferred maintenance expense.

The Company further complains that Mr. Radigan did not identify any specific maintenance project that should be postponed or canceled in order to maintain the annual expense level he thought should be constant over time. According to the Company, the AG failed to provide any factual basis for its assumption that all maintenance can be staggered so the future expense should be based on the same number of projects at the same cost as in past years. USI Exhibit 5.2 identifies the Company's Policy and Maintenance Guidelines associated with its Asset Management Program underlying the timing of the deferred maintenance projects. The Company argues maintenance schedules are affected by a diverse set of factors, including among other things, the nature of the maintenance, age and type of facility or equipment being maintained, climate, extent of deterioration from varying demands placed on the assets, improved asset management techniques and budgeting constraints. The Company contends that the AG's recommendation did not examine or assess any aspect of the Asset Management Program. Accordingly, the Company urges the Commission to reject the AG's recommendation.

b. AG's Position

The AG argues that given the large number of water and sewer facilities owned by the Company, it should be doing several deferred maintenance projects like painting, testing, and inspecting each year, and its annual expense should be constant over time. AG Ex. 1.0 at 12. However, the AG contends that the Company's projected deferred maintenance expense is almost double that of 2014 and approximately four times greater than what was incurred in 2009, 2010, and 2011. *Id.* at 13. According to the AG, the Company did not show any reason for such a dramatic increase. Thus, AG witness Radigan recommended that the Company should only be allowed recovery of \$300,000 for deferred maintenance, which is over 20% higher than the 2014 actual expense amount of \$245,000. *Id.* at 13.

The AG states that while Staff witness Bridal's recommendation to reduce deferred maintenance expense by almost \$200,000 is very close to the amount of Mr. Radigan's proposed adjustment, Mr. Bridal's proposal is based on a different theory. The reduction recommended by Mr. Bridal is based primarily on an adjustment that extends the amortization period on certain tank painting projects from five years to ten years. Staff Ex. 1.0 at 17; Staff Sched. 1.14 W at 1; Tr. at 72. The AG asserts that Mr. Bridal admitted during cross-examination that his proposal to lengthen the amortization period on tank painting will not preclude USI from recovering those costs; it merely stretches out the period for recovering the costs. Tr. at 75. The AG adds that Mr. Bridal took no consideration of the number of proposed tank painting projects in the 2015 test year against the historic average of such projects. Tr. at 76. The AG concludes that it does not object to the Commission adopting Mr. Bridal's extended amortization period. However, because Mr. Bridal's adjustment makes no attempt to consider the justness and reasonableness of the amount of the Company's proposed cost recovery for deferred maintenance, the AG argues that the Commission should adopt Mr. Radigan's proposed adjustment in addition to Staff's recommended adjustments.

With respect to USI's position, the AG notes that the Company argues that Mr. Radigan's proposed adjustment should be rejected because he failed to identify any unnecessary projects and he did not conduct any inspections of the facilities in question. The AG contends that USI's argument flips the burden of proof on its head because the Company bears the burden of establishing the just and reasonableness of its proposed rates pursuant to Section 9-201(c) of the Act and USI failed to meet its burden.

c. Intervenors' Position

The Intervenors note that although the AG and Staff recommended different approaches to reduce deferred maintenance expense, the final numbers reached by both parties were within a few thousand dollars. Thus, the Intervenors state that they do not oppose the Company's revised expense level of \$294,440, which reflects its acceptance of Staff's adjustments, since it is nearly identical to the AG's proposed reduction. USI Ex. 12.0 at 9.

d. Staff's Position

Staff proposed three adjustments to deferred maintenance expense and deferred charges. Staff proposed an adjustment to remove deferred volatile organic compound

testing costs that were incurred prior to the test year and for which the Commission did not authorize the deferral as required by 83 Ill. Adm. Code 605, the Uniform System of Accounts in Illinois, Instructions to Account 186, Miscellaneous Deferred Debits. Staff also proposed an adjustment to remove the cost of painting the Company logo on tanks. Staff explains that this adjustment was made because: (1) painting the Company logo on tanks is not necessary for the provision of utility services; (2) the costs to paint the Company logo on tanks are incurred for promotional, institutional, or goodwill advertising which is not permitted under the Act; and (3) recovery of the costs incurred to paint the Company logo on tanks is contrary to Commission guidance in its Final Order in the Company's most recent rate case. Finally, Staff changed the amortization period for tank painting from the Company-proposed period of five years to ten years, thereby reducing the amount of deferred maintenance expense included in the revenue requirement. Staff argues that ten years is a more reasonable length of time between tank paintings because it is consistent with the amortization period that has been requested by the Company in prior rate cases and consistent with the amortization period approved by the Commission in prior rate cases. Staff Ex. 1.0 at 13-17.

Staff agrees with AG witness Radigan in that the Company's forecasted level of deferred maintenance expense for the test year was beyond what should be expected. Staff observes that its analysis and resulting adjustments removed specific, non-recoverable costs in addition to extending the amortization period for various tank painting projects from five years to ten years, consistent with prior Commission practice. *Id.* These adjustments reduced water deferred maintenance expense for the test year by \$199,896. Staff Ex. 1.0, Sched. 1.14 W. Staff explains that while its adjustment to extend the amortization period for tank painting projects reduced test year tank painting amortization expense, these adjustments also increased deferred charges in rate base by \$459,640. *Id.* The net effect of Staff's adjustments to deferred maintenance and deferred charges was to reduce the revenue requirement requested by the Company for its water service areas by \$154,583. Staff Ex. 1.0, Sched. 1.05 W.

Staff takes issue with the AG's assertion that Staff makes no attempt to consider the justness and reasonableness of the amount of the Company's proposed cost recovery for deferred maintenance, but instead only proposes to stretch out the recovery of the same costs over a longer period. Staff argues that this statement mischaracterized Staff's position and it is incorrect, as Staff witness Bridal proposed adjustments which disallowed several deferred maintenance costs because the deferrals had not been authorized by the Commission, were not necessary for the provision of utility services, or were not permitted under the Act. Staff Ex. 1.0 at 13-16. Thus, Staff asserts that it did consider the justness and reasonableness of the amount requested by the Company for deferred maintenance.

Staff states that the AG is correct that one component of Mr. Bridal's adjustment to extend the amortization period for tank painting from five years to ten years does extend the recovery of the same costs over a longer period. However, Staff notes that the ten year amortization period is consistent with both the Company's and the Commission's prior practice. Staff Ex. 1.0 at 16-17. Staff further notes that the AG does not object to Mr. Bridal's reasoning regarding the extended amortization period.

Staff maintains that for the reasons set forth above, the Commission should adopt its adjustments to deferred maintenance expense and deferred charges.

e. Commission Analysis and Conclusion

As noted by the Intervenor, Staff and the AG are in agreement that the Company's forecasted level of deferred maintenance expense for the test year was beyond what should be expected. Although Staff and the AG recommended different approaches to reduce this expense, they both reached similar results. The Commission agrees with these parties that the deferred maintenance expense should be adjusted downward. Based on a review of the record, the Commission finds that Staff's proposed adjustments are supported by the evidence, reasonable, and should be adopted. Contrary to the AG's assertions, Staff's analysis shows that it considered whether the amount requested by the Company was just and reasonable. Staff identified specific costs that should be disallowed because the deferrals had not been authorized by the Commission, were not necessary for the provision of utility service, and were not permitted under the Act. Moreover, its adjustment, which the AG does not object to the Commission adopting, to extend the amortization period for tank painting projects is consistent with both the Company's and the Commission's prior practice. For these reasons, the Commission adopts Staff's adjustments, which were accepted by the Company, and declines to approve any further reductions proposed by the AG.

2. Rate Case Expense – WSC Personnel

a. Company's Position

USI asserts that its revenue request includes the costs of WSC employees who performed the work necessary to file and obtain Commission approval of new rates. These costs were supported by time records maintained by WSC employees, which were admitted into the evidentiary record. USI Ex. 7.2 (Part 1); USI Ex. 13.2 (Part 1). Those records identify the employees who performed the work, provide a description of the work performed, and show the amount of time spent. USI contends that the same type of information was provided to the Commission in Docket Nos. 12-0603/12-0604 (Consol.). Both Staff and the Commission found that the utilities in those cases had provided sufficient information to support the recovery of WSC employee costs as part of rate case expense. USI Ex. 12.0 at 10. Consequently, USI asserts, the AG's argument that the Company has not provided sufficient support for the recovery of costs of internal personnel who worked on this rate case is unfounded.

USI avers that the AG's argument with respect to the accounting for rate case expense attributable to WSC employees is the same argument that was previously reviewed and rejected by Staff in Docket Nos. 11-0059/11-0141/11-0142 (Consol.) and Docket Nos. 11-0561 through 11-0566 (Consol.). In the latter proceeding, Staff reviewed the Company's method of accounting for internal employee costs related to rate cases and verified it ensured no double counting of internal labor in rate case expense and test year labor charges.

According to the Company, the test year operating expenses allocated to USI for WSC wages and salaries do not include any amounts for employees working on rate cases because those employees charge that time directly ("cap time") to the particular

company, as they are required to do by the Affiliated Interest Agreement (“AIA”) approved by the Commission. Those direct charges are subtracted from the amount of operating expenses that are allocated to operating companies such as USI. In other words, the residual amounts allocated to USI and other UI affiliates include no directly assigned expense for work performed by employees on rate cases. USI points out that its exhibits show the amount of cap time reductions. The Company reduced its expenses by \$112,028 for rate case cap time. USI Ex. 3.2 at 1. Thus, the Company contends the reductions are not mere “bald assertions” as claimed by the AG. They are backed up by the books and records of the Company, which reflect the time reported by employees as cap time.

b. AG’s Position

The AG argues that USI did not establish that certain WSC employees’ salaries are not included in both rate case expense and wages and salaries expense. AG witness Radigan observed that without a showing that there is no double counting of internal staff time allocated to both wages and salaries expense and rate case expense, all rate case expense costs should be excluded from the test year revenue requirement. AG Ex. 2.0 at 18. The AG asserts that because USI failed to show that there is no double counting, the AG recommended that the Commission adopt Mr. Radigan’s recommendation that the internal staff component of rate case expense be removed from the test year revenue requirement – a downward adjustment of one-fifth of \$195,470, or \$39,094. AG Ex. 1.0 at 10.

The AG contends that USI’s assertion that the Commission rejected the AG’s argument concerning double counting before in Docket Nos. 11-0561 through 11-0566 (Consol.) is erroneous. The AG submits that the Commission did not address this argument because the companies did not provide enough evidence to establish that their proposed rate case expense was just and reasonable. *Charmar Water Company, et. al.*, Docket Nos. 11-0561 through 11-0566 (Consol.), Final Order at 20 (May 22, 2012). The AG notes that the Commission stated that it was mindful of the double counting concern raised by the AG, but it did not address that issue, because “[t]he Commission cannot make an informed judgment regarding that initial “single”-counting of these labor expenses, as that information is not in the record.” *Id.*

c. Staff’s Position

In direct testimony, Staff proposed an adjustment to reduce rate case expense from WSC. Staff explains that this adjustment was recommended because the Company’s supporting documentation was only minimally descriptive of the duties performed and of the number of hours spent for each duty. Staff Ex. 2.0 at 6. Staff points out that USI’s rebuttal testimony included an update to its actual and estimated rate case expense, which included more detailed descriptions of time spent by WSC employees. USI Ex. 7.0 at 5.

Staff accepted the detailed listing of time spent by WSC employees provided by USI in its rebuttal testimony and withdrew its adjustment in rebuttal testimony. Staff Ex. 8.0 at 4.

d. Commission Analysis and Conclusion

The Commission does not believe that the AG's proposed adjustment to disallow rate case expense attributable to WSC personnel is warranted. The record shows that the Company has provided detailed information regarding what actual expenses were incurred, by whom, for what purpose, and why such expenses were necessary to either prepare the case, respond to discovery, prepare testimony, or complete other activities pertinent to the case. The Company also included a reasonable estimate of the costs to bring the case to conclusion. The information provided by the Company is consistent with past Commission practice, notably Docket Nos. 12-0603/12-0604 (Consol.).

The Commission agrees with the Company that there is no evidence of double counting. As the Company stated, the exhibits provided by USI show the amount of cap time reductions. Specifically, they show that the Company reduced its expenses by \$112,028 for rate case cap time. It is also noteworthy that the AG itself admitted in direct testimony that USI included a 50% reduction to salaries related to rate case activities in 2015.

Moreover, the Commission has considered the costs expended by the Company, as discussed in this Section and Section III.A.9, to compensate attorneys and technical experts to prepare and litigate this rate case proceeding and assesses that such costs in the total amount of \$738,522, which is \$147,704 amortized over five years, are just and reasonable pursuant to Section 9-229 of the Act. 220 ILCS 5/9-229.

3. Insurance Expense

a. Company's Position

The Company states that its proposed revenue request for insurance expense included a share of the common insurance expense forecasted to be incurred by WSC. The total costs of the entire UI organization across all states were forecasted to decline by 2.2% between 2014 and 2015. USI explains that the costs were allocated to all UI operating companies on the basis of the number of equivalent residential connections ("ERCs") each utility has. This allocation is required by the AIA approved by the Commission. Thus, the Company states that while the total insurance expense was forecasted to decrease, USI's share of those costs would increase because the UI's system-wide decrease was offset by the larger share of the costs that were required by the AIA to be allocated to USI. USI Ex. 14.0 at 7.

USI explains that it provided a table in its surrebuttal testimony to better explain the increase to insurance expense that shows: a WSC overall insurance expense decline of 2.2%, consistent with its explanation in USI Exhibit 3.1; an increase in USI's ERC base of 2.5%; and the resulting 0.3% increase in USI's allocation of WSC insurance expense between 2014 and 2015. USI Ex. 14.0 at 2-3.

USI takes issue with the AG's proposed adjustment and urges the Commission to reject the adjustment. According to USI, the AG opposes the amount of insurance expense included in the Company's revenue request because the AG failed to verify how the amount was calculated. USI contends that the AG's adjustment fails to incorporate WSC's current insurance policies and using a historical average of insurance costs, as

the AG's adjustment proposes, is not reflective of USI's current operating conditions. USI Ex. 14.0 at 8.

b. AG's Position

The AG claims that the Company's forecast should be rejected because the numbers do not add up. AG witness Radigan testified that USI's insurance expense increased from \$187,804 in 2014 to a projected \$196,978 in the 2015 future test year, a 4.88% increase. AG Ex. 1.0 at 10-11. The AG highlights that according to USI, its share of WSC's insurance costs for all of the UI subsidiaries increased from 6.90% to 7.07%, a 2.46% increase. USI Ex. 14.0 at 2. However, the AG asserts that USI provided no explanation as to how a 2.46% increase in its share of overall WSC insurance costs coupled with a 2.2% decrease in WSC overall insurance costs yields an almost 5% increase in insurance expense for the Company.

The AG also claims that USI's evidentiary presentation concerning insurance costs was part of a pattern the Company followed in this case on several issues. According to the AG, USI presented minimal information supporting certain increased expenses in its direct case. When Staff and/or the AG challenged some of those expenses in their respective direct cases, USI provided additional information regarding the challenged items. When Staff and/or the AG argued that the additional information was not sufficient, USI provided even more detail in its surrebuttal case. The AG argues that is precisely what USI did with insurance expense. The AG asserts that the Commission should not reward such "hide-the-ball" tactics. Utilities should be required to submit all supporting information in their direct cases. Moreover, the AG contends that Staff and the Intervenor should not have to expend scarce resources extracting additional information from utilities for explanations that purportedly support their requested rate increases.

The AG states that while the information submitted in USI's surrebuttal testimony satisfied Staff's concerns about this issue, the additional information did not satisfy the AG's concerns. The AG maintains that the Company did not meet its burden of proof on this issue. It recommends that the Commission reject USI's proposed test year expense level and adopt the proposal made by Mr. Radigan, which uses the \$174,525 two-year average as the test year insurance expense in the Company's revenue requirement.

c. Staff's Position

Staff states that in rebuttal testimony it supported the AG's proposed adjustment to decrease the Company's forecasted insurance expense for the 2015 test year, but changed its position later upon review of the Company's surrebuttal testimony. Staff explains that in rebuttal testimony it agreed with the AG's theoretical basis in its direct testimony for an adjustment to insurance expense, but did not agree with using the average of 2013 and 2014 insurance expense to determine the adjustment. Staff instead proposed reducing USI's insurance expense by 2.2% to match the forecast basis USI provided in USI Exhibit 3.1 (Guidelines for 2014-2015 Forecast) that showed WSC would experience a 2.2% decrease in cost between 2014 and 2015. Staff notes that USI challenged these adjustments and stated in its rebuttal testimony that: "Total allocated costs to USI do not decrease between FY 2014 and FY 2015 because of incremental allocations related to the acquisition of USI's Oakwood system." USI Ex. 8.0 at 6-7.

Staff asserts that it subsequently withdrew its adjustment based on the detailed table USI presented in its surrebuttal testimony to better explain the increase to insurance expense.

d. Commission Analysis and Conclusion

The Commission finds that the Company has provided adequate support for its increase in insurance expense for the 2015 test year. The Company explains, that pursuant to the cost allocation formula in the AIA approved by the Commission, common expenses such as insurance, are required to be allocated to affiliated operating utilities based upon the number of ERCs. Thus, the total allocated costs to USI do not decrease between 2014 and 2015 because of its incremental allocations related to the acquisition of USI's Oakwood system. As illustrated in the table presented by the Company in surrebuttal testimony, USI's customer base in 2015 is a larger percentage of UI's customer base than in 2014, thus the Company will not experience the 2.2% decrease forecasted for WSC but rather it will experience a slight increase in insurance expense due to the increase in its share of the total UI customer base. Like Staff, the Commission is satisfied with this explanation of the Company's increase in insurance expense.

Additionally, the Commission agrees with the Company that adjusting this expense by using USI's 2013 to 2014 average insurance expense, as proposed by the AG, is not reasonable. 2013 to 2014 allocated costs do not reflect UI's or USI's current customer base, and it is therefore a poor predictor of USI's anticipated costs for the test year. Moreover, 2013 to 2014 costs do not reflect the anticipated level of insurance expense to be incurred by WSC. Therefore, the Commission declines to adopt the AG's recommendation to use the two-year average as the test year insurance expense instead of the Company's forecast which is based on current and projected insurance policies.

4. Wages & Salaries Expense – WSC Personnel

a. Company's Position

The Company explains that it calculated its wages and salaries expense forecast based on current and anticipated levels of staffing for 2014 and 2015. USI challenges the AG's proposal to use the most recent 18-month period available, January 2013 through June 2014, as a basis for setting the net salaries and wages expense level for the test year revenue requirement.

According to USI, the AG's recommendation is flawed because it fails to identify any position that should be eliminated or any misallocation of the costs that it believes exists in the Company's accounting records. AG witness Radigan relied on historical levels without considering additional staffing related to the recent acquisition of the sewer and water systems that serve the Village of Oakwood as well as the incremental allocations that would result from the increase in ERCs that drive the allocation of common costs in accordance with the AIA. USI Ex. 8.0 at 7. USI argues that the AG's recommendation is also problematic because it would ignore the 3% annual base pay increases that have and are anticipated to occur. In addition, Mr. Radigan's analysis also fails to incorporate the filling of vacant positions. *Id.* The Company maintains that the use of historical expense levels as Mr. Radigan recommended would defeat the purpose

of a future test year and destine the Company to repeat the financial results that the Company's accounting records show fail to produce an adequate return on investment.

b. AG's Position

The AG alleges that the Company's proposed wages and salaries expense is overstated. AG witness Radigan explained that wages and salaries expense is comprised of two components: (1) salaries and wages and (2) maintenance expense charged to plant. AG Ex. 1.0 at 14. He explained that salaries and wages are the payroll costs for a company and maintenance expense charged to plant is employee time spent on a project that is capitalized and as wages and salaries expense become part of the project over time. *Id.* at 14. Mr. Radigan further explained that net wages and salaries expense is calculated by subtracting the maintenance expense charged to plant from salaries and wages.

The AG points out that for its 2015 test year, the Company is forecasting a net wages and salaries level of \$1,133,588, a 45% increase over the annualized value from the most recent 18-month period available. *Id.* at 15-16. As to the wages and salaries component, the AG notes that the Company projects a forecasted increase from \$1.226 million to \$1.684 million – a 37% increase, far in excess of a 3% annual labor cost increase. AG Ex. 1.0 at 16.

The AG contends that USI's explanations for its proposed increase in wages and salaries expense are meritless. The AG asserts that the Company did not prove that the Oakwood acquisition increased its headcount. AG Ex. 2.0 at 17. Mr. Radigan also found, that salary expense has been flat over the past five years, despite salary increases during that time. *Id.* at 17. Further, the AG states that for ten particular employees, the Company is requesting a portion of their time to be recovered under salaries and wages and the same portion to be recovered under rate case expense. *Id.* at 16-17.

Additionally, the AG states that USI has not met its burden of proof. The Company's entire argument in the AG's view is a critique of Mr. Radigan's alleged failures to conduct additional discovery or to review information provided which does not satisfy the Company's obligation to prove its case.

For these reasons, the AG recommends that the Commission adopt Mr. Radigan's proposal to use the most recent 18-month period available, January 2013 through June 2014, as a basis for setting a net wages and salaries expense level for the test year. This results in an expense level of \$781,934 for the test year revenue requirement. AG Ex. 1.0 at 17.

c. Commission Analysis and Conclusion

The Commission finds that the Company has provided sufficient information to justify its anticipated future test year wages and salary expense. The Commission agrees with the Company that the AG's reliance on historical averages fails to consider the additional staffing related to the acquisition of USI's Oakwood system, the incremental allocations from the increased percentage of USI's ERC's, an anticipated 3% annual base pay increase, and the filling of vacant positions. The record shows that the Company provided detailed explanations for the increase in salary and wages expense and detailed projections of salary expense for each employee in its forecast. Additionally, as stated in

Section III.B.2(d) concerning rate case expense attributable to WSC personnel, there is no evidence of double counting. Thus, the Commission declines to adopt the AG's proposed adjustment.

5. Uncollectibles Expense

a. Company's Position

The Company states that its uncollectible expense was determined based on its records of the following accounts: (1) agency expense, (2) uncollectible accounts expense and (3) uncollectible accounts accrual expense. The Company explains that all three accounts must be included in the calculation of uncollectible expense. The Company further explains that agency expense is the cost of engaging collection agencies to attempt collection of bad debts. Uncollectible account expense consists of the net of accounts written off and payments on previously written off balances. Uncollectible accounts accrual expense represents costs that are accruals for anticipated account balance write-offs. USI Ex. 8.0 at 4-5.

The Company states that the AG's argument that uncollectible accounts accrual expense should not be included in the calculation of uncollectible expense is incorrect. The Company asserts that to accurately assess the amount of uncollectible expense experienced by the Company, uncollectible accounts accrual expense must be included because the Company's accounting system automated processes only captures account balance write-offs when the service disconnection event is entered into the system. The Company explains that availability customers do not receive service. Because availability customers cannot be disconnected, uncollectible accounts expense only reflects the automatic write-offs triggered by disconnection and fails to account for the significant uncollectible account expense associated with customers who fail to pay availability charges.

USI further states that when all necessary components are utilized, uncollectible percentages forecasted for the test year are consistent with USI's actual experience in past years. USI Ex. 8.0 at 4-5. The Company points to its surrebuttal testimony which it maintains illustrated the significant growth in aged accounts receivable attributable to availability customers. According to the Company, its analysis determined that 95% of these balances over 181 days delinquent are unlikely to be paid and therefore should be written off. USI Ex. 14.0 at 4-6. The Company states that it will fail to achieve the target revenues necessary to cover the costs of providing service unless these write-offs are reflected in the uncollectible expenses the Company is allowed to recover in its rates. Accordingly, the Company asserts that the AG's adjustment should be rejected because it fails to address uncollectible expense associated with delinquent availability customers or agency expense.

b. AG's Position

AG witness Radigan proposed to reduce the USI total water and sewer uncollectible expense by \$79,149 to \$30,000, roughly equal to recent averages. AG Ex. 1.0 at 7. In support of his adjustment, Mr. Radigan testified that he found that the Company's absolute bad debt expense (also known as "net write offs") varies widely from year to year and the Company's forecast grossly overstated uncollectible expense on a

percentage basis. AG Ex. 1.0 at 6-7. The AG notes that Mr. Radigan later updated his adjustment to \$31,400 in his rebuttal testimony to include agency expense. AG Ex. 2.0 at 8.

The AG disputes the Company's assertion that Mr. Radigan's proposed adjustment should be rejected because he refused to consider uncollectible accounts accrual expense. The AG argues, citing Mr. Radigan's testimony, that the decision whether to increase uncollectible accounts accrual expense is discretionary and if that account is rising while accounts receivable is steady, the company is putting too much in reserve, which is precisely what USI is doing. *Id.* at 9-10. According to the AG, the Company's level of accounts receivable has been relatively steady from 2009 to 2014, while the Accumulated Provision for Uncollectable Accounts has almost tripled between 2008 and 2014.

Mr. Radigan testified that the Company has sufficient money in the Accumulated Provision for Uncollectible Accounts to stop setting aside any money in the uncollectible accounts accrual and to bring the Accumulated Provision for Uncollectible Accounts back down to the 2008 level (from almost \$300,000 in 2014 to \$100,000 in 2008). The AG asserts that because bad debt expense has averaged approximately \$30,000 per year, this draw down could occur for as long as five years with no more uncollectible accounts accrual. Accordingly, the AG submits that contrary to the Company's assertions, uncollectibles accounts accrual should not be included in this case because it will result in a windfall to the Company. *Id.* at 10.

c. Staff's Position

Staff states that it agrees with AG witness Radigan that the USI absolute bad debt expense varies widely from year to year and the percentage of absolute bad debt in comparison to revenues is lower than the uncollectible percentage proposed by the Company in this proceeding. However, Staff asserts that it does not agree with the AG's adjustment.

Staff notes that in determining its proposed uncollectible percentage in this proceeding, USI divided its forecasted Account 670 Bad Debt Expense amount by its forecasted test year operating revenues. Staff argues this approach is consistent with the approach approved by the Commission in the Company's prior rate case filings. Staff Ex. 7.0 at 9-10. In addition, as noted in the rebuttal testimony of USI witness Kersey, when calculated using consistent methodologies, the uncollectible percentages proposed by the Company in this proceeding are consistent with the Company's recent historical experience. USI Ex. 8.0 at 5. Staff further argues that Mr. Radigan's adjustment does not appear to account for the presence of significant uncollectible amounts associated with unpaid availability charges. USI Ex. 14.0 at 4-5.

Staff recommends that the Commission approve total water and sewer test year uncollectible expense as 1.08% of approved operating revenue, as proposed by the Company. As explained above, 1.08% is consistent with the Company's recent experience, is calculated consistently with the methodology approved by the Commission in the Company's prior rate case filings, and reflects uncollectible amounts associated with unpaid availability charges. Staff asserts that should the Commission disagree with Staff and the Company and adopt Mr. Radigan's proposal, then the Commission should

ensure that the AG adjustment is apportioned between water and sewer service using ERC counts set forth within Staff Cross Exhibit 1.

d. Commission Analysis and Conclusion

The Commission agrees with Staff and the Company that the AG's proposed adjustment to exclude uncollectible accounts accrual expense should be rejected. The Company's forecasted uncollectible expense of 1.08% is reasonable and supported by the record evidence.

As Staff explained, the Company calculates its uncollectible expense by determining an uncollectible percentage and multiplying that uncollectible percentage by its proposed revenues. In determining its proposed uncollectible percentage in this case, the Company divided its forecasted Account Bad Debt Expense amount by its forecasted test year operating revenues. This calculation is consistent with the methodology approved by the Commission in the Company's prior rate case filings. Moreover, the Company's forecast of 1.08% is consistent with the Company's recent historical experience and reflects the significant uncollectible amounts associated with delinquent availability customers. Accordingly, the Commission concludes that all three accounts noted by the Company must be included when determining the Company's uncollectible expense.

6. Sales Adjustment

a. Company's Position

The Company asserts that the Commission should adopt its forecasted test year sales level, which reflects a 2.65% decline in customer usage. The Company explains that from August 2008 to July 2014, USI saw an average annual decline in consumption of 2.65%. According to the Company, the data buttresses the conclusion that the trend will continue and the test year consumption should be reduced by 2.65%. The Company contends that the failure to account for declining use would impede its ability to earn its authorized return and necessitate more frequent requests for rate relief, which would add additional rate case expense to be recovered from customers. USI Ex. 1.0 at 12. The Company's witnesses cited examples of industry studies, reports, executive orders, and other government policies that indicate a pervasive trend toward lower water usage per household. USI Ex. 6.0 at 11-14.

USI takes issue with AG witness Radigan's recommendation that the Commission should reject the six years of data showing annual consumption declines. Mr. Radigan suggested the decline might be attributable to increasingly wetter weather. The Company argues that the AG's position is without merit. The Company asserts that the only weather information the AG provided was rainfall isolated to a part of the Company's service area in the far northwestern corner of the state. This information is unpersuasive since the Company also has service areas located in northeastern and central Illinois. The Company further asserts that its usage data spans across six years and so any variations in weather are likely to offset each other. Moreover, the Company maintains that the AG presented no evidence that the weather patterns over those six years were unusual, abnormal or unlikely to repeat over the next five years that the new rates will be in effect. In addition, the consumption decline also occurred in the non-summer periods when

rainfall and temperature would be expected to have little impact on water use. Tr. at 51. The Company contends that the steady decline in the non-summer months over the six year period strongly supports the prospect of the continued drop in test year consumption due to factors such as improved efficiency measures, conservation consciousness, and demand response to higher costs.

The Company also argues that the AG's reference to the bivariate correlation of 0.25 cited in USI Exhibit 8.0, Schedule 8.3 cannot be used to support the AG's proposition that consumption and rainfall have a negative correlation. The Company asserts that the 0.25 correlation is a positive correlation meaning it implies higher rainfall would coincide with higher consumption. Therefore, USI Exhibit 8.0, Schedule 8.3 actually supports the Company's testimony that the AG's witness has "made inaccurate and misleading statements regarding the correlation and causation between rainfall and consumption." USI Ex. 8.0.

For these reasons, USI urges the Commission to reject the AG's recommendation to exclude the expected decline in consumption in the calculation of rates.

b. AG's Position

The AG states that the Commission should reject the Company's adjustment to reflect a 2.65% decrease in customer usage. The AG argues that USI has not proved that such a decrease is warranted because the Company has not normalized its recent sales data against rainfall over the same time period. The AG asserts that consumption and rainfall have a negative correlation; USI witness Kersey's own analysis found a bivariate correlation of 0.25 between these two variables. USI Ex. 8.0, Sched. 8.3. Moreover, as AG witness Radigan showed, Galena, Illinois, for example, has seen generally higher rainfall than normal during the past five years. AG Ex. 1.0 at 7-10. The AG argues that such a finding is consistent with high rains driving lower usage. A six-year sample of sales is predictive of future sales only if the rainfall and temperature during the six-year sample were consistent with average rainfall and temperature over a longer time period. AG Ex. 2.0 at 4-5. The AG contends that the Company did not prove that in its presentation.

The AG adds that Mr. Kersey admitted in cross-examination that the Company did not prepare any multivariate regression analysis attempting to include both temperature and rainfall as explanatory variables driving consumption. Tr. at 42. In re-direct examination, Mr. Kersey stated that the Company "look[ed] at the six-year weather" over the same time period and "compared those to "10, 20, and 100-year averages for both rainfall and temperature, and did not see any abnormalities or a reason to adjust the consumption for weather." However, the AG highlights that upon cross-examination, Mr. Kersey admitted that "abnormality" in his telling meant a deviation greater than five percentage points from long-term historic averages and that it is likely that he would have ignored any deviation from normal of less than five percentage points when examining rainfall over the past six years. *Id.* at 48, 50. The AG argues that a deviation of 4.9%, then, would have escaped Mr. Kersey's attention – but such a deviation would swamp the alleged 2.65% decline in usage, meaning that his examination of the representativeness of recent rainfall trends had little value.

The AG concludes that USI failed to meet its burden of proving that its projected sales decrease is just and reasonable. Accordingly, the AG recommends that the Commission use the actual 2014 sales level, without any reduction, as the test year billing determinants in setting new rates to achieve the approved revenue requirement.

c. Intervenor's Position

The Intervenor concurs with the AG that the Commission should reject the Company's adjustment to reflect a 2.65% decrease in customer usage. The Intervenor asserts that USI's argument concerning this issue is unconvincing. They contend that the Company engaged in a debate with AG witness Radigan about whether the sales adjustment should be a rate design or revenue requirement issue instead of providing a factual basis for the adjustment. Further, the Intervenor maintains that if the Company's adjustment is adopted it will result in a higher charge per unit rate, thereby allowing USI to reap the benefits of overstating the amount sales might decrease. In addition, the Intervenor asserts that the Company's adjustment should also be rejected because it provided no analysis or study supporting its hypothesis that a 2.65% water usage/sales decrease would continue in the future.

d. Staff's Position

Staff asserts that the Commission should reject the sales adjustment proposed by AG witness Radigan. Staff explains that it appears Mr. Radigan proposed an adjustment to increase current revenues by \$130,000, which he maintains will then reduce the total revenue requirement by \$130,000. AG Ex. 1.0 at 10. However, Staff claims that Mr. Radigan's proposed adjustment, in the form he has proposed it, would not reduce the final total revenue requirement in the way that Mr. Radigan intends.

Staff witness Bridal explained how the total revenue requirement is calculated on his Schedule 1.01 W. Staff Ex. 1.0 at 4. Because of the way the total revenue requirement is calculated in column (i) of this schedule, Mr. Radigan's adjustment would not change the final total revenue requirement because the final revenue requirement is calculated using the approved rate base, return on rate base, and operating expenses. Mr. Radigan's adjustment would merely increase the current revenues shown in column (d) by \$130,000 and decrease the adjustment to the proposed amount in column (h) by an offsetting \$130,000. Staff argues this would leave the total revenue requirement in column (i) unchanged and fail to accomplish what Mr. Radigan intends.

Staff states that it does not object to the Company's adjustment to reflect a 2.65% decrease in customer usage. However, if the Commission agrees with Mr. Radigan that it is unreasonable to anticipate any decline in usage, then Staff recommends that the Commission increase the usage billing units by 2.65% in the calculation of rates rather than adjusting the revenues in the manner Mr. Radigan proposes. Staff notes that the AG acknowledged in its Initial Brief that if an adjustment is made, then it should be made to the usage billing units used to calculate the final rates to recover the approved revenue requirement.

e. Commission Analysis and Conclusion

The Commission finds that the AG's position that USI's consumption levels should not be adjusted to reflect the Company's projected decrease in customer usage of 2.65%

is unpersuasive. USI has provided ample support for its projected decrease in water consumption for the 2015 test year, including six years of historical data from 2008 to 2014 showing annual consumption declines. The Company also provided industry studies, reports, executive orders, and other governmental policies indicating a trend throughout the industry toward lower water usage. Additionally, the Company presented a demonstration that shows weather normalization is unnecessary in this situation where the Company's analysis includes several years of data since any variations in the weather during this time period are likely to offset each other. Finally, the AG asserts that one of the main drivers of water use is rainfall, however, the AG failed to provide convincing evidence to support this position. The AG also failed to refute the historical data provided by the Company or to show that it is unreasonable to expect that the decline in water consumption will continue in the future. For these reasons, the Commission declines to adopt the AG's proposal and the Company's forecasted test year sales level, which reflects a 2.65% decline in customer usage, is approved.

C. Commission Conclusions on Operating Revenues and Expense Statement

The development of the approved water operating expense statement for USI in this proceeding is shown in Appendix A to this Order, while the approved sewer operating expense statement is shown in Appendix B to this Order. The Commission finds that the adjustments to the operating expense statements reflected in the appendices are supported by the evidence, are reasonable, and should be adopted.

IV. RATE OF RETURN

A. Capital Structure

Staff and the Company agree that USI's capital structure for the year ended December 31, 2015 is comprised of 1.74% short-term debt, 47.96% long-term debt, and 50.30% common equity. USI Ex. 11.0, Sched. 11.1.

B. Cost of Debt

Staff estimated that the Company's cost of short-term debt is 1.69%, based on the current interest rate on USI's short-term revolving bank facility. Staff Ex. 5.0 at 8. The Company's embedded cost of long-term debt for 2015 is 6.66%. Staff Ex. 5.0, Sched. 5.3. Staff included the annual amortization of debt expense, which reflects straight-line amortization of the unamortized balance over the remaining life of the outstanding issue of long-term debt. Staff Ex. 5.0 at 8.

USI accepted Staff's costs of short-term and long-term debt. USI Ex. 11.0, Sched. 11.1.

C. Return on Equity

For the purpose of resolving the issue, the parties have agreed to a 9.25% return on equity ("ROE") for USI for the purpose of setting rates. Staff Ex. 10.0 at 1; USI Ex. 11.0 at 2. Staff's Initial Brief noted that the decision to agree with a 9.25% ROE should not be construed to mean that Staff witness Freetly concluded that any adjustment proposed by Company witness D'Ascendis to Ms. Freetly's cost of common equity

analysis had merit. Staff Ex. 10.0 at 1. A 9.25% ROE was recommended by the AG and is within the range of results produced by various methodologies used by Staff and the Company. USI Ex. 11.0 at 2.

Given the above, the Commission approves an ROE of 9.25% for USI.

D. Commission Analysis and Conclusion

Having reviewed the record, the Commission finds that the Company should be authorized to earn a rate of return of 7.88%. The rate of return incorporates a return on common equity of 9.25%. The Company's rate of return was derived as follow:

<u>Source of capital</u>	<u>Amount</u>	<u>Percentage</u>	<u>Cost</u>	<u>Weighted Cost</u>
Short-term debt	\$6,496,098	1.74%	1.69%	0.04%
Long-term debt	\$178,726,842	47.96%	6.66%	3.19%
Common Equity	<u>\$187,444,000</u>	<u>50.30%</u>	<u>9.25%</u>	<u>4.65%</u>
Total	\$372,666,940	100.00%		7.88%

V. RATE DESIGN

A. Uncontested Issues

1. Availability Charges

The Company proposed an availability charge of \$1.68, in its initial filing, which indicates that the Company proposes to bill availability customers only the actual \$1.68 cost that it takes to send them a monthly bill. Staff Ex. 4.0 at 15.

Staff opined that charging availability customers a monthly amount that is equal to the cost of sending them a monthly bill was not appropriate. Although availability customers are not currently using water, they have the ability to avail of such service, just as full water customers do, and they should be required to pay a fee for that service privilege. According to its filing, the Company allocates approximately 11.4% of its operation and maintenance costs to availability customers. Furthermore, these customers currently pay an amount for availability service that is more than the cost of sending them a monthly bill. *Id.* at 15-16.

According to the Staff witness, the average monthly availability charge currently is approximately \$8.50 for all divisions with availability customers. Charging this rate would generate approximately 6% of the overall yearly revenue for the Company and would represent a fair portion of the contribution to revenues based on the availability of service and the approximately 11.4% of operations and maintenance costs allocated to serve these customers. Full water customers have to pay a monthly base facilities charge for the privilege to have water service available to them. Availability customers should similarly share in some of the monthly costs that the Company incurs to provide water service to all customers. *Id.* at 16. The Company indicated that it would accept the \$8.50 consolidated availability charge, which is reflected in its rebuttal schedules. USI Ex. 6.0 at 6.

Intervenors who are located in service areas not presently subject to availability charges submitted testimony in opposition to application of the availability charge on a

statewide basis. The Company responded by providing testimony to clarify that its intent was to continue the availability charge only in the services areas where the charges are currently in effect, and the tariffs will be modified accordingly.

The Commission finds that Staff's proposed availability charge, which shall apply only in those service areas currently paying availability charges, is reasonable and should be adopted.

2. Provision of an Updated Cost of Service Study in the Company's Next Rate Case

For its cost of service study ("COSS"), the Company used the simplified cost of service study model that Staff provided previously, which is designed for small water companies. For purposes of this case, the Company's COSS appropriately assigns costs to the various functions and rate classes. Thus, it is an acceptable guidance tool for determining rates in this case. Staff Ex. 4.0 at 25.

However, Staff witness Boggs testified that a more comprehensive COSS would likely provide a better snapshot of how the cost to serve all customers should be allocated to the different customer classes across the current water divisions and sewer divisions. Mr. Boggs recommended that the Commission order the Company to provide in its next rate case a full, in-depth COSS along the lines of those presented in the American Water Works Association's Water Rates Manual M1, Sixth Edition. This would assist in determining the most equitable way to allocate costs and expenses among the various customer classes in the consolidated group. *Id.* at 26.

The Company indicated that it will provide a COSS consistent with the American Water Work's Association's Water Rates Manual M1, Sixth Edition. The Company further explained that it would need to engage an expert to perform the study and would expect the cost of doing so to be subject to recovery as rate case expense. USI Ex. 6.0 at 7.

The Commission agrees with Mr. Boggs' recommendation.

B. Contested Issues

1. Consolidated Rate Structure

a. Consolidation of All Service Areas

(i) Company's Position

The Company proposes to combine: (1) its water divisions into one consolidated water division that has a single rate structure and (2) each of its sewer divisions into one consolidated sewer division that has a single rate structure.

Company witness Lubertoizzi indicated that consolidated rates are commonplace in other regulated utilities like gas and electric. He testified that consolidated rates would allow USI to spread capital costs over a larger base of customers, thus mitigating rate shock to a smaller stand-alone division's customer base when infrastructure improvements become necessary in a particular rate area. He also indicated that, in the long-term, consolidated rates will strengthen USI and allow the customers to enjoy lower rates via fewer rate cases and lower rate case expense. USI Ex. 1.0 at 13.

The Company disagrees with the Intervenor's position that the Commission should reject the Company's proposals or in the alternative phase the rates in over several rate cases. The Company argues that the Intervenor failed to provide any specific alternative rates that should be adopted for each stand-alone service area in lieu of the uniform rates supported by the Company and Staff. More importantly, the preservation of differing rates for the separate service areas would defeat the primary purposes of the consolidation, which were to create a broader customer base over which to distribute recovery of costs and to alleviate the rate impacts associated with multiple rate proceedings that would otherwise be needed for smaller, stand-alone companies.

Additionally, the Company avers that the Intervenor oppose the consolidation proposals primarily because they have become accustomed to stand-alone rates that are below the Company-wide cost of service. The Company points out that it is true that the Intervenor will experience an increase in their rates if the proposed consolidated rate structure is approved but it is also true that customers in service areas where stand-alone rates are higher than the Company-wide cost of service will experience a decrease in their rates. Thus, the consolidation proposals will ensure that all customers make an equal contribution to the recovery of the system-wide cost of service.

Moreover, USI claims that the Intervenor exaggerate the impact of rate consolidation by focusing exclusively on the percentage of the increase for customers in the Galena Territory and Westlake Utilities service areas, and completely avoid mentioning the actual dollar amount of the monthly bills under the consolidated rates. The dollar impact is considerably more moderate than the percentage increase would suggest. Under the revenue requirement recommended by Staff, a 5/8" customer using 3,000 gallons of water per month would have a monthly water bill of \$41.86, and a monthly sewer bill of \$47.35. Further, the Intervenor cite public comments that express concerns about the perceived negative impact of the percentage increase on low and fixed income customers in these service areas. However, a lower percentage increase for the Intervenor would require a compensating increase that would impact low and fixed income customers in service areas that are currently paying much more than the consolidated rates. The Company states that the consolidated rate structure assures the affordability of the rates is the same for all USI customers.

Finally, the Company submits that the Commission should decline to adopt the Intervenor's alternative recommendation to phase-in the consolidation of rates over several rate cases. USI asserts that this proposal would take 15 years based on the time between rate cases upon which the amortization of rate case has been based in this case. Additionally, the Intervenor ignore the administrative costs associated with maintaining 23 different sets of rates and applying the changes in multiple steps over years.

Accordingly, the Company asserts that the Commission should reject the Intervenor's arguments and approve the Company's proposed consolidated rate structure.

(ii) Intervenor's Position

The Intervenor object to the Company's consolidation proposals. They claim that Staff provided testimony that the consolidated rate structure will result in a rate increase that exceeds the costs to serve the average water customers of the Galena Territory,

Westlake Utilities, and Lake Holiday divisions. According to the Intervenor, if water rates were based on the costs to serve these customers, the rate increases to average users served by the Galena Territory division would be 23.3%, not the 45% increase proposed. For the Westlake Utilities division, if rates were based on the cost to serve, the increase would be 78%, not the 159% increase proposed. For the Lake Holiday division, if rates were based on costs, the increase would be 40%, not the 110% proposed.

The Intervenor asserts that these draconian increases, are contrasted with the dramatic decreases in water rates that other divisions would see as a result of the proposed rate consolidation. For example, customers served by the Charmar Water division would see a nearly 65% decrease, the Del-Mar Water division would see a 55% decrease, and the Camelot Utilities division would see a decrease of 30%. The Intervenor states that USI and Staff attempt to justify this disparity by alleging that, the Company's proposals would benefit customers because in the future if a small division would need to add facilities, the increase to all customers would be less than what would be imposed on the division causing the costs to be incurred. The Intervenor argues that this is not a valid reason to adopt rates that are not reasonable, cost-based, or fair to customers. The public comments filed in this docket by ratepayers themselves, which the ALJ must review, show that ratepayers do not understand or accept that their water rates will increase by 50% to 160% under the Company's consolidated rate structure when the cost to serve those customers justifies a rate increase of only half that amount.

If the Commission permits water rates that are not cost-based, then the Intervenor suggests that system-wide water rates be set at a level where no USI ratepayer receives an average bill increase in excess of the system-wide rate increase for water service. In the alternative, if the purpose is to eventually move all of the divisions to one state-wide rate, then the Intervenor maintains that the movement should be done incrementally to avoid the rate shock caused by increasing some water rates by 160% while giving other customers decreases of over 60%. The Intervenor also recommends that if the Commission approves an incremental movement to state-wide rates, any increase to an individual division's rates should not exceed the cost of service as listed in Staff witness Boggs' testimony. Staff Ex. 4.0 at 7.

The Intervenor also objects to consolidating the wastewater rates. They argue that these proposed rates are not supported by any evidence since, as Staff noted, USI did not conduct a COSS to calculate the uniform wastewater rate. In addition, the proposed consolidation would result in the average bill for the Galena Territory division to increase by 145% and for Westlake Utilities division to increase by 52%. And as with water rates, the consolidated wastewater rate would conversely result in significant decreases for other divisions, for example, a 45% decrease for the Northern Hills Water and Sewer division and 27% decrease for the Camelot Utilities division. For these reasons, the Intervenor asserts that if the Commission adopts wastewater rates that are not cost-based, then the Intervenor proposes that any increase to specific wastewater divisions be limited to an increase of no more than the system-wide rate increase for wastewater service.

(iii) Staff's Position

Staff recommends that the Commission approve the Company's consolidation proposals. Staff witness Boggs reviewed information that the Company included in its initial filing and considered bill impacts for average use customers. Staff explains that Mr. Boggs did this to determine what the rate impacts of a consolidated rate structure would be on each individual water division. Mr. Boggs' initial review indicated that, only seven divisions (Clarendon Water, Ferson Creek Utilities, Galena Territory, Killarney Water, Lake Holiday, Whispering Hills, and Westlake Utilities) would receive a higher increase under the Company's proposed consolidated rate structure than they would receive on a stand-alone basis. He testified that customers of all seven of the above mentioned water divisions would see a significant increase whether they remain a stand-alone division or whether they are consolidated with other divisions in any combination. Staff Ex. 4.0 at 5-7.

Mr. Boggs also explored several different rate structure combinations based on the bill impact scenarios and determined that some should be further analyzed. Based on his analysis, he concluded that pulling any division out of the fully consolidated group as a stand-alone group might mitigate the rate impacts to the stand-alone group, but the remainder of the consolidated group would have more significant rate impacts. However, Mr. Boggs testified that this must be weighed against the fact that, for all the water divisions, large capital improvements could be spread among a larger base of customers when it becomes necessary to update infrastructure to provide safe and reliable water service. According to Mr. Boggs, consolidation would also mitigate the impact of rate case expenses if the Company has to file for only a single division rather than more numerous stand-alone water divisions. When rate case expenses and infrastructure improvements are necessary, significant rate increases to fund these improvements could prove quite burdensome for the small number of customers in individual, smaller water divisions. Thus, Mr. Boggs further testified that the long-term benefits of consolidation outweigh its costs. *Id.* at 12-13.

Staff challenges the Intervenor's assertion that by establishing statewide rates that exceed the stand-alone cost to serve customers, USI's rates to customers served by the Galena Territory and Westlake Utilities divisions are neither just nor reasonable. Staff argues that contrary to the Intervenor's assertion, the determination of whether a rate is just and reasonable under the Act does not solely depend upon a cost analysis as the Intervenor argues. The Intervenor fails to recognize that the Act allows the Commission to consider factors other than costs when designing rates. Under the Act, one of the goals and objectives of regulation is to consider equity. 220 ILCS 5/1-102(d). Equity is the fair treatment of consumers and investors. *Id.* Staff explains that equity involves not just considering the cost of supplying service so that it is allocated to those who cause the costs, 220 ILCS 5/1-102(d)(iii), but it can include factors other than cost of service. 220 ILCS 5/1-102(d)(iv) (stating "if factors other than cost of service are considered in regulatory decisions, the rationale for these actions is set forth").

Staff highlights that Company witness Lubertozzi and Staff witness Boggs provided equitable justification for the Commission to approve a single consolidated rate rather than stand-alone rates. Staff notes that Mr. Lubertozzi testified that consolidated rates are common place for other regulated entities like gas and electric. USI Ex. 1.0 at 13.

He explained the benefits of costs being spread over a larger base; how the consolidated rate will strengthen USI; and how the consolidated rate will allow customers to benefit from fewer rate cases and lower rate case expense. *Id.* at 282-288. Mr. Boggs agreed in general with Mr. Lubertozi's testimony on this issue and his justification for the consolidated rate structure is noted above. Staff Ex. 4.0 at 5.

Staff mentions that the Intervenor's quote many comments made by customers of the Galena Territory and Westlake Utilities divisions that are posted on the Commission's website in the public comments section for this docket. The Intervenor's argue that the comments show that customers do not understand the proposed increases and that the rates are unreasonable, and to help those customers better understand the increases and utility charges, they should be phased-in over several rate cases, eventually culminating in a single consolidated rate. Staff asserts that putting aside whether the fact that customers do not understand a rate or believe a rate is unreasonable is a sufficient basis to justify a phase-in given the equity goal and objective in Section 5/1-102(d)(ii) of the Act, the Commission is free to reject a phase-in. It clearly is within the Commission's discretion to approve a single consolidated rate in this case, as the Company proposes and Staff supports. Staff further asserts that the courts give great deference to the Commission in setting rates and the courts have held that "because of its complexity and need to apply informed judgment, rate design is uniquely a matter for the Commission's discretion." See *Iowa-Illinois Gas & Electric Co. v. Illinois Commerce Comm'n*, 19 Ill. 2d 436, 442, 167 N.E.2d 414 (1960); *Central Illinois Public Service Co. v. Illinois Commerce Comm'n*, 243 Ill. App. 3d 421, 445, 610 N.E.2d 1356, 183 Ill. Dec. 112 (1993).

Based upon the above, Staff contends that the Commission should reject the Intervenor's arguments for a phase-in and approve the Company's proposed consolidated rate structure.

(iv) Commission Analysis and Conclusion

The Commission finds that the Company's consolidated rate structure is reasonable, supported by the evidence, and should be adopted. The Commission declines to adopt the phase-in recommended by the Intervenor's.

As of the date of this Order, 599 public comments were posted on the Commission's e-Docket system regarding the consolidated rates proposed by USI. The Commission appreciates these comments as well as the time and effort expended by those who prepared and provided them. These comments have not been taken lightly and they have been carefully considered by the Commission to the extent permitted by law. The Commission is very much aware that the comments express strong opposition to the proposed rate increases, however, they do not overcome the evidence supporting the proposed consolidated rates. Moreover, the Commission is of the opinion that the benefits of the rate consolidation outweighs the disadvantages.

As Staff stated, cost of service is not the only consideration that may be used to determine whether rates are just and reasonable. Contrary to the Intervenor's arguments, the Commission is permitted under the Act to consider many factors other than costs when designing rates. Under the Act, one of the goals and objectives of regulation is to consider equity, which is the fair treatment of customers and investors. 220 ILC 5/102(d). The Commission believes the consolidation proposals advance this objective. The record

shows that only seven of the twenty-two water divisions reviewed by Staff will experience a higher increase under the Company's proposed consolidated rate structure than they would receive on a stand-alone basis. All of these divisions will experience a significant increase in rates whether they are a stand-alone division or consolidated with other divisions in any combination. Staff Ex. 4.0 at 5-7. Further, many of the customers in these divisions, including Galena Territory, Lake Holiday, and Westlake Utilities, have been charged stand-alone rates that are below the Company-wide cost of service and the customers in the divisions identified by the Intervenor that will experience a decrease in rates have been charged rates that exceed the Company-wide cost of service. Thus, a consolidated rate structure will address this disparity and ensure that all customers make an equal and appropriate contribution to the recovery of the system-wide cost of service.

The Commission also notes that Staff's analysis of several different rate structure combinations based on bill impact scenarios shows that removing any division from the consolidated group as a stand-alone group might mitigate the rate impacts to the stand-alone group, but the remainder of the consolidated group would have significant rate impacts. Additionally, the consolidated rate structure moves USI closer to the rate structure most common for other regulated utilities. It will allow the Company to spread capital costs over a larger base of customers, thus mitigating rate shock to a smaller stand-alone division's customer base when infrastructure improvements are necessary. It would also alleviate the rate impacts associated with multiple rate proceedings that would otherwise be needed for smaller, stand-alone divisions.

Finally, the Commission believes the Intervenor have not provided sufficient support to show that their recommendation that the consolidated rates should be phased-in over several rate cases is a better approach. The phase-in would delay the Company's recovery of its costs of service for an unreasonable amount of time since it could take up to 15 years to phase-in the consolidated rates. There was no evidence provided concerning the impact of the administrative costs related to maintaining different sets of rates and applying the changes in multiple steps over the years. Moreover, the Intervenor did not include specific alternative rates for each stand-alone service area in its recommendation to use instead of the uniform rates supported by the Company and Staff.

b. Inclusion of Oakwood in Rate Design

(i) Company's Position

The Company explains that it purchased the Oakwood division's water and wastewater operations through an Asset Purchase Agreement ("APA") dated September 9, 2013 from the Village of Oakwood. The transaction was approved by the Commission through a Certificate of Public Convenience and Necessity in Docket No. 13-0564 on March 19, 2014. Under the APA, the Company agreed to continue to charge the current rates for a period of two years. Thereafter, rates were to be charged consistent with the Company's consolidated rate schedule as approved by the Commission.

The Company asserts that it included Oakwood in the consolidated group's revenue requirement in the Company's direct testimony even though Oakwood's rates remain unchanged because of the rate freeze in the APA. The Company states that Oakwood would in effect be subsidized by the consolidated group because Oakwood is

included in the total revenue requirement, but its rates are not revised to reflect that revenue requirement.

USI points to the two alternatives offered by Staff witness Boggs to address Oakwood's subsidization by the consolidated group. The first suggestion was that Oakwood could be removed from the consolidated group's revenue requirement and rates entirely. This would ensure that the consolidated group's rates reflected only the consolidated group's revenue requirement. A second alternative was suggested by the Company in its responses to a Staff data request. Under this alternative, the Company would seek to unify the Oakwood service area rates and revenue requirement with the rest of the consolidated group when the restriction on rates charged to customers in the Oakwood service area expires. This would be accomplished by leaving Oakwood in the consolidated group's revenue requirement, calculating consolidated rates for all USI customers including Oakwood, but not applying the consolidated group's rates to Oakwood customers until March 10, 2016 when the rate freeze expires. The Company explains that Oakwood customers would continue to pay the current Oakwood rates until March 10, 2016. This would create a revenue requirement shortfall with respect to the Oakwood rates until March 10, 2016. The Company indicates that this shortfall would be a shareholder expense and would not be passed on to customers.

(ii) GTA's Position

GTA witness Mattingley expressed concern about the effect USI's acquisition of the Oakwood division might have on the water and wastewater rates for the Galena Territory division. He specifically requested information concerning what costs attributable to Oakwood are included in Galena Territory's rates to GTA and its members, and what benefits, if any, Galena Territory achieved for Galena by acquiring a system over 200 miles from the city. GTA Ex. 1 at 3-4. In rebuttal testimony, Mr. Mattingley continued to express concern about including Oakwood as part of Galena Territory. GTA Ex. 2 at 3. He stated that he was not completely satisfied with USI's response that there are costs included from all 23 operating areas in all customer's rates.

(iii) Staff's Position

Like the Company, Staff included Oakwood in the consolidated group's revenue requirement in its direct testimony and determined that Oakwood would in effect be subsidized by the consolidated group, including the Galena Territory division. As previously noted, Staff witness Boggs offered two alternatives to address this issue. He stated that both alternatives would adequately address the subsidization issue, but the alternative suggested by the Company, which would add the Oakwood service territory to the rest of the consolidated group would provide certain advantages. USI Ex. 13.0 at 5-7.

Mr. Boggs testified that the primary advantage that the Oakwood service area water customers would realize from being included in the consolidated group is having a larger customer base to spread capital improvement costs over when large infrastructure investments and repairs are needed. In addition, Oakwood's usage charge would decrease by \$0.01 per 1,000 gallons. Moreover, the Company would avoid another rate case in a year to determine the rates that would be needed to recover the new revenue requirement for the Oakwood service area. Mr. Boggs explained that with only 737 water

customers, rate case expense for those customers would further increase the rates that would be needed to recover the revenue requirement that will eventually be determined. Staff Ex. 9.0 at 7.

Mr. Boggs stated that the chief advantage to all Oakwood sewer customers from consolidation is the ability to spread future capital expenses and rate case expenses over a larger group of customers, thereby mitigating future bill impacts. In addition, the sewer rates would also decrease by \$2.45 per month on a flat-rate basis. *Id.* at 8.

Accordingly, Staff recommends that the Commission approve this approach because of the advantages identified by Mr. Boggs.

(iv) Commission Analysis and Conclusion

The Commission concurs with Staff and the Company that the best way to address the potential for Oakwood to be subsidized by the consolidated group is the alternative suggested by the Company. This option would entail adding the Oakwood service territory to the rest of the consolidated group but not applying the consolidated rates to Oakwood customers until March 10, 2016 when the rate freeze expires. This approach would not unfairly impact other customers since the shortfall would be borne by shareholders and it would not be passed on to customers. Additionally, it would be beneficial to Oakwood customers because future capital improvement costs and rate case expenses could be spread over a larger group of customers, thereby mitigating future bill impacts. Further, if this alternative is adopted, the Company would not have to file another rate case in a year to determine the rates that would be needed to recover the new revenue requirement for the Oakwood service area.

VI. OTHER

A. Elimination of Purchased Water and Purchased Sewer Surcharges

The Company proposed to eliminate all of its purchased water surcharges and purchased sewer surcharges and to include the costs of all purchased water and purchased sewer services within base rates. Inclusion of the costs of all purchased water and sewer services within base rates is consistent with the Company's proposal to establish a consolidated rate structure for its customers, and eliminates the need for annual purchased water and purchased sewer reconciliation proceedings. USI Ex. 1.0 at 12-13; USI Ex. 2.0 at 7-8.

Staff recommends that the Commission approve the Company's proposal to eliminate its purchased water and purchased sewer surcharges, subject to Staff's proposed language and Commission approval of a new transition/clean up tariff which provides for the final reconciliations of purchased water and purchased sewer surcharges, as discussed in Section VI.B. below. Staff Ex. 1.0 at 17-19; Staff Ex. 7.0 at 11-14. The Company agrees with Staff's conditions. USI Ex. 7.0 at 10-11.

The Commission finds the Company's proposal, as modified by Staff's conditions, to be reasonable.

B. Final Reconciliations of Purchased Water and Purchased Sewer Surcharges

As discussed in Section VI.A. above, the Company agrees with Staff's recommendations and conditions concerning the Company's proposal to eliminate all of its purchased water surcharges and purchased sewer surcharges. USI Ex. 7.0 at 10-11.

In the event that the Commission approves the Company's proposal to eliminate all of its purchased water surcharges and purchased sewer surcharges and to include the costs of all purchased water and sewer services within base rates, the Commission should adopt Staff's recommendations as follows:

- The final order in this proceeding should authorize and require USI to include with its compliance filing in this proceeding, tariff sheets consistent with the proposed language on page 12 of Staff Exhibit 7 that:
 - provide a mechanism for the reconciliation of purchased water and sewer costs and revenues for any reconciliation periods that have not yet been considered by an order of the Commission;
 - provide a mechanism for the refund or recovery of any cumulative (over)/under recovery determined from those reconciliations; and
 - provide for the disposition of any Factor Os ordered by the Commission that result from the proceedings to reconcile the revenues and expenses of each surcharge that have not yet been considered by the Commission at the time an order is entered in this proceeding;
- The final order in this proceeding should require the Company to file, within 90 days of the final order in this proceeding, a petition for a final reconciliation of the USI purchased water and purchased sewer surcharges for the year 2015 up to the effective date of new tariffs filed in compliance with the final order in this proceeding; and
- The final order in this proceeding should include the following language in the Ordering paragraphs:

IT IS FURTHER ORDERED that within 90 days of the date of this Order, Utility Services of Illinois, Inc. shall for the period from January 1, 2015, through the effective date of new tariffs filed in accordance with this Order, file a final reconciliation of its purchased water and purchased sewer surcharges, along with a petition requesting approval of said reconciliation which includes testimony and schedules that support the accuracy of the costs and charges for the period being reconciled.

The Commission finds Staff's recommendations are reasonable and Staff's recommended language should be included in the Findings and Ordering paragraphs.

C. Proposed Depreciation Rates

USI witness Guastella provided a depreciation study utilizing comparable data for average service lives, net salvage values, depreciation rates of other water and sewer utilities, as well as state and industry guidelines. USI Ex. 4.0 at 6. Mr. Guastella proposed separate water and sewer depreciation rates for each primary account. USI Ex. 4.0, Scheds. JFG-1 and JFG-2.

Staff witness Sperry did not object to the Company's depreciation study or the proposed depreciation rates. Staff Ex. 6.0 at 5.

The Commission approves the sewer and water depreciation rates proposed by the Company.

D. Maximum Allowable Unaccounted-for Water Percentage

USI proposed to combine all of the Company's existing percentages of maximum unaccounted-for water, without changes, into a single tariff sheet for all of its service areas. USI Ex. 2.0 at 11.

Staff witness Sperry recommended that the maximum level of unaccounted-for water for the four service areas (Clarendon Water, Great Northern, Walk-Up Woods, and Westlake Utilities) be reduced to 15% in USI's revised Schedule of Rates and Charges tariffs for water service. Staff Ex. 6.0 at 9. The Company accepted Staff's recommendations.

The Commission adopts Staff's recommended maximum levels of unaccounted for water.

E. Other Tariff Change Proposals

In anticipation of the Commission's approval of the Company's consolidation proposals, the Company proposed several changes to its tariffs. In its Unaccounted for Water tariff, the Company condensed the existing percentages applicable to the various service divisions into a single sheet (ICC No. 3, Original Sheet No. 4.). In its Schedule of Rates tariff, the Company has created uniform miscellaneous charges that it derived from its current tariffs in each service territory. The Company also proposed to change all service divisions to a monthly billing cycle. This will make all the service divisions' billing cycles consistent with each other and with the billing cycles that the Commission has been approving in recent individual rate cases for the utility company's predecessor. Staff Ex. 4.0 at 34.

Staff recommends that the Commission approve the Company's tariff change proposals. Doing so will make the tariffs uniform if the Commission approves the consolidated rate structure.

Approving the proposed tariff changes would add consistency and uniformity to each service division's individual tariff. Therefore, the Company's proposed changes are reasonable and the Commission approves these proposals.

VII. FINDINGS AND ORDERING PARAGRAPHS

The Commission, having given due consideration to the entire record herein and being fully advised in the premises, is of the opinion and finds that:

- (1) USI provides water and sewer service to the public within the State of Illinois, and, as such, is a public utility within the meaning of the Act;
- (2) the Commission has jurisdiction over USI and of the subject-matter herein;
- (3) the recital of facts and conclusions reached in the prefatory portion of this Order are supported by the evidence, and are hereby adopted as findings of fact;
- (4) a test year ending December 31, 2015, should be adopted for the purpose of this rate proceeding;
- (5) the \$37,241,560 original cost of water plant in service for USI at December 31, 2013, as reflected on Staff's Schedule 1.15 W, is unconditionally approved as the original costs of plant;
- (6) the \$11,760,334 original cost of sewer plant in service for USI at December 31, 2013, as reflected on Staff's Schedule 1.15 S, is unconditionally approved as the original costs of plant;
- (7) a fair and reasonable rate of return on the rate base for USI is 7.88%; rates should be set to allow the Company an opportunity to earn that rate of return on its rate base, as is determined herein;
- (8) the rates which are presently in effect for USI are insufficient to generate the operating income necessary to permit the Company to earn a fair and reasonable rate of return; those rates should be permanently canceled and annulled as of the effective date of the new tariffs allowed by this Order;
- (9) the rates proposed by USI would produce a rate of return in excess of a return that is fair and reasonable; the Proposed Tariffs of Utility Services of Illinois, Inc. should be permanently canceled and annulled;
- (10) pursuant to Section 9-229 of the Act, the Commission has specifically assessed the amounts expended by the Company to compensate attorneys and experts to prepare and litigate this general rate case filing and finds those amounts, as adjusted, to be just and reasonable, with the Commission's more detailed supporting findings on this subject as set forth in this Order;
- (11) USI should be permitted to file new tariff sheets setting forth the rates designed to produce operating revenues as shown in Appendix A and B as such revenues are necessary to provide the Company a rate of return of 7.88% on their rate base, consistent with the findings herein; these tariff sheets shall be applicable to service furnished on or after their effective date;
- (12) USI shall also file new tariff sheets consistent with the proposed language set forth on page 12 of Staff Exhibit 7 as discussed in Section VI.B. of this

Order concerning final reconciliations of purchased water and purchased sewer surcharges;

- (13) the new tariff sheets authorized to be filed by this Order shall reflect an effective date not less than five working days after the date of filing, with the tariff sheets to be corrected within that time period if necessary, except as is otherwise required by Section 9-201(b) of the Act as amended;
- (14) USI shall file, within 90 days of the date of this Order, a petition for a final reconciliation of the USI purchased water and purchased sewer surcharges for the year 2015 up to the effective date of new tariffs filed in compliance with the Order in this proceeding;
- (15) all remaining motions, petitions, objections, or other matters in this proceeding should be disposed of in a manner consistent with the conclusions reached herein; and
- (16) USI shall otherwise perform all actions that this Order requires of it.

IT IS THEREFORE ORDERED by the Commission that the tariff sheets proposing a general increase in water rates filed by Utility Services of Illinois, Inc. on November 10, 2014 are hereby permanently canceled and annulled.

IT IS FURTHER ORDERED that Utility Services of Illinois, Inc. is authorized to place into effect tariff sheets which will produce the annual operating revenues and operating incomes set forth in the Findings above, and are consistent with Appendices A and B to this Order, to be effective on the date of filing for water and sewer service furnished on and after such effective date.

IT IS FURTHER ORDERED that Utility Services of Illinois, Inc. shall also place into effect tariff sheets consistent with the proposed language set forth on page 12 of Staff Exhibit 7 as discussed in Section VI.B. of this Order concerning final reconciliations of purchased water and purchased sewer surcharges;

IT IS FURTHER ORDERED that Utility Services of Illinois, Inc. must file its Rate tariffs consistent with the requirements of the Findings above.

IT IS FURTHER ORDERED that upon the effective date of the tariff sheets filed pursuant to this Order, the presently effective tariff sheets of Utility Services of Illinois, Inc., which are replaced thereby are permanently canceled and annulled.

IT IS FURTHER ORDERED that within 90 days of the date of this Order, Utility Services of Illinois, Inc. shall for the period from January 1, 2015, through the effective date of new tariffs filed in accordance with this Order, file a final reconciliation of its purchased water and purchased sewer surcharges, along with a petition requesting approval of said reconciliation which includes testimony and schedules that support the accuracy of the costs and charges for the period being reconciled.

IT IS FURTHER ORDERED that any petitions, objections or motions made in this proceeding and not otherwise specifically disposed of herein are hereby disposed of in a manner consistent with the conclusions contained herein.

IT IS FURTHER ORDERED that the \$37,241,560 original cost of water plant in service for Utility Services of Illinois, Inc. at December 31, 2013, as reflected on Staff's Schedule 1.15 W, is unconditionally approved as the original costs of plant.

IT IS FURTHER ORDERED that the \$11,760,334 original cost of sewer plant in service for Utility Services of Illinois, Inc. at December 31, 2013, as reflected on Staff's Schedule 1.15 S is unconditionally approved as the original costs of plant.

IT IS FURTHER ORDERED that, subject to the provisions of Section 10-113 of the Public Utilities Act and 83 Ill. Adm. Code 200.880, this Order is final; it is not subject to the Administrative Review Law.

DATED:

August 7, 2015

BRIEFS ON EXCEPTIONS DUE:

August 21, 2015

REPLY BRIEFS ON EXCEPTIONS DUE:

September 4, 2015

Sonya Teague Kingsley,
Administrative Law Judge